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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF SECRETARY

April 15, 1994

Mr. William F. Caton
Acting Secretary
Federal Communications Commission
1919 M Street, N.W.
Washington, D.C. 20554

Re: Ex parte written presentation in MM Docket No. 92-265

Dear Mr. Caton:

Enclosed is a written Ex parte presentation on behalf of our client, Home Box Office ("HBO"), in response to the previous Ex parte written presentations by the National Rural Telecommunications Cooperative ("NRTC") in the above-captioned proceeding.

HBO addresses NRTC's claim that the program distribution contract between the United States Satellite Broadcasting Co., Inc. ("USSB"), a direct broadcast satellite ("DBS") distributor, and HBO violates the 1992 Cable Act's program access provisions. As demonstrated herein, the 1992 Cable Act does not prohibit exclusive contracts between programmers and DBS operators. Moreover, the HBO/USSB contract promotes consumer access to programming and enhances competition.

Copies of this Ex parte presentation and this letter are being sent to the individuals listed on the following page. Please feel free to contact me if you have any questions.

Sincerely,

Michael H Ham

Michael H. Hammer

enclosure

No. of Copies rec'd 0+2
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John B. Richards
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BEFORE THE

Federal Communications Commission

WASHINGTON, D.C.

In the Matter of	)	
	)	
Implementation of Sections 12 and 19 of the Cable Television Consumer Protection and Competition Act of 1992	)	MM Docket No. 92-265
	)	
Development of Competition and Diversity in Video Programming Distribution and Carriage	)	

Ex Parte Response of Home Box Office To Ex Parte Presentations of the National Rural Telecommunications Cooperative

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Its Attorneys

April 15, 1994

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SUMMARY

Contrary to assertions made by the National Rural Telecommunications Cooperative ("NRTC"), the direct broadcast satellite ("DBS") program distribution contract between Home Box Office ("HBO") and the United States Satellite Broadcasting Company, Inc. ("USSB") does not violate § 628 of the Communications Act of 1934, as amended.

The language of the Act makes clear that § 628 is limited to arrangements made between programmers and cable operators. The Conference Report, the most persuasive evidence of Congressional intent, states unequivocally that § 628 prohibits:

> exclusive contracts and other arrangements between a cable operator and a vendor...

The Department of Justice has concluded that § 628:

> prohibits exclusive arrangements between program vendors and cable operators, but does not expressly prohibit such arrangements between programming vendors and a non-cable firm such as USSB.

Moreover, the HBO/USSB agreement promotes the public interest. The agreement provides for multiple retail distributors and thus ensures that consumers in all geographic areas will have access to HBO's services from multiple sources. The agreement also is pro-competitive. The agreement provides for very limited exclusivity. It does not give USSB exclusivity against MMDS, SMATV, C-band satellite distributors, cable operators, DBS distributors at other orbital slots, or video dialtone providers. It also allows USSB to distinguish its

product from its rivals, thus increasing USSB's ability to compete with a well-heeled rival that has significantly larger channel capacity.

Finally, as described below, HBO has legitimate, pro-competitive business reasons for entering into the limited exclusivity contract with USSB.

For these reasons, the Commission should reject NRTC's assertion that the HBO/USSB agreement violates § 628 of the Act.

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Ex Parte Response of Home Box Office To Ex Parte Presentations of the National Rural Telecommunications Cooperative

The National Rural Telecommunications Cooperative ("NRTC") has filed two Ex Parte presentations[1] alleging that the exclusivity provisions of the DBS program distribution contract between Home Box Office ("HBO") and the United States Satellite Broadcasting Co. ("USSB") violate Section 628 of the Communications Act of 1934, as amended.[2] As demonstrated below, the language and legislative history of Section 628, as well as established public policy principles, refute NRTC's position.

As an initial matter, HBO urges the Commission to consider NRTC's position in light of the fact that NRTC sought to

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[1] NRTC's initial Ex Parte presentation was filed on November 19, 1993 (hereinafter "NRTC November 19 Ex Parte"). NRTC filed a subsequent Ex Parte presentation on March 4, 1994 (hereinafter "NRTC March 4 Ex Parte").

[2] Section 19 of the Cable Television Consumer Protection and Competition Act of 1992 ("1992 Cable Act") added Section 628.

establish itself as the sole retail provider of HBO's services in the NRTC service areas.[3] NRTC's approach would have been more limiting of consumer choice than the exclusive right contained in the HBO/USSB agreement which, as explained below, provides for multiple retail distributors in all geographic areas.

I. The 1992 Cable Act Does Not Prohibit Exclusive Contracts Between Programmers and DBS Operators

In its November 19 Ex Parte filing, NRTC incorrectly asserts that Section 628(c)(2)(C) prohibits all exclusives in non-cabled areas."[4] In quoting the 1992 Cable Act, however, NRTC omitted language demonstrating that Congress' intention was to limit exclusivity in certain contracts between programmers and cable operators. Section 628(c)(2)(C) provides for Commission rules as follows (the language NRTC omitted is underlined):

> prohibit practices, understandings, arrangements, and activities, including exclusive contracts for satellite cable programming or satellite broadcast programming between a cable operator and a satellite cable programming vendor or satellite broadcast programming vendor, that prevent a multichannel video programming distributor from obtaining such programming...[5]

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[3] It is HBO's understanding that NRTC entered into an agreement with DirecTv giving NRTC the exclusive right to distribute certain program services in the NRTC service areas. DirecTv initially sought the exclusive right to distribute HBO which, in turn, would have given NRTC exclusive distribution rights for HBO within its service areas.

[4] NRTC November 19 Ex Parte at ¶18 (emphasis original).

[5] Section 628(c)(2)(C); 47 U.S.C. § 548(c)(2)(C).

In effect, NRTC urges the Commission to interpret Section 628(c)(2)(C) as imposing a duty on programmers to sell to all distributors in areas not served by cable. NRTC's argument is that every distributor, without restriction, has an absolute right to distribute HBO's services in such areas. Under NRTC's theory, HBO would have no right to determine the distribution of its product in non-cable areas.

There is no language in Section 628 or any indication in the legislative history to support so radical an interpretation. Moreover, NRTC's interpretation is belied by the legislative history of the 1992 Cable Act. The Act, as originally introduced in the House, expressly stated that exclusive contracts which denied multichannel video programming distributors access to programming in rural areas not served by cable "shall be construed to be an unreasonable refusal to deal."[6] However, this provision was deleted from the final version of the Act. The Commission should not, as NRTC urges, interpret Section 628 as if the deleted provision had been included in the Act.[7]

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[6] H.R. 4850, 102d Cong., 2d Sess. § 11(a)(3).

[7] Without explanation, NRTC also asserts that Sections 628(b) and 628(c)(2)(B) prohibit the HBO/USSB exclusivity arrangement. NRTC March 4 Ex Parte at 10, n. 7. While HBO disputes that these sections prohibit its agreement with USSB, NRTC's self-serving position demonstrates the weakness of its interpretation of Section 628(c)(2)(C). NRTC repeatedly states that Section 628(c)(2)(C) unequivocally bans "all exclusive arrangements in areas unserved by cable." See NRTC March 4 Ex Parte at 9 (emphasis original); see also id., at 12, 13, 22. If NRTC's broad and definitive interpretation of Section 628(c)(2)(C) were correct, it would have been superfluous for Congress to have covered the same conduct in Sections 628(b) and 628(c)(2)(B).

The legislative history of the Act makes clear that Section 628(c)(2)(C) is limited to exclusive distribution arrangements between vertically integrated programmers and cable operators. The Conference Report conclusively states:

> With regard to areas not passed by a cable system, <u>the regulations required by the House amendment prohibit exclusive contracts and other arrangements between a cable operator and a vendor</u> which prevent a multichannel video programming distributor from obtaining programming from a satellite cable programming vendor affiliated with a cable operator.[8]

It is a settled principle of statutory construction that the Conference Report is the most important element of legislative history in interpreting the meaning of a statute: "Since the conference report represents the final statement of terms agreed to by both houses of Congress, next to the statute itself, it is the most persuasive evidence of Congressional intent."[9]

In response to the unequivocal language in the Conference Report that Section 628(c)(2)(C) deals only with exclusive contracts involving a cable operator, NRTC cites several comments from the House floor debate.[10] But none of the comments NRTC cites deal with the issue NRTC has raised in this proceeding. The comments address general matters, such as whether cable operators have market power, or the extent of support for the

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[8] H.R. Conf. Rep. No. 862 102d Cong., 2d Sess. 92 (1992) (emphasis added).

[9] 2A Norman J. Singer, <u>Sutherland Statutory Construction</u> § 48.08 (5th ed. 1992) and cases cited therein.

[10] NRTC March 4 <u>Ex Parte</u> at 15-18.

Tauzin amendment among cable's competitors. NRTC does not cite a single instance in the legislative history where the issue of exclusivity between programmers and DBS operators was discussed. That is because the legislative history contains no such discussion.

NRTC attached a June 16, 1993, letter from Congressman Billy Tauzin to its March 4 Ex Parte presentation which expressed Congressman's Tauzin's views on the exclusivity provisions in Section 628 of the Act. However, Congressman Tauzin's letter was written after passage of the Act and "[p]ostpassage remarks by legislators, however explicit, cannot serve to change the legislative intent expressed prior to an act's passage."[11]

For the same reason, the March 1, 1994, letter from members of the Congressional Rural Caucus of the U.S. House of Representatives to Chairman Hundt concerning the exclusivity provisions in Section 628 cannot override the clear interpretation articulated in the Conference Report. Moreover, the concern expressed in the Rural Caucus letter that exclusivity arrangements between programmers and DBS operators would deny programming to rural Americans is inapplicable to the HBO/USSB agreement. One of HBO's chief concerns is that all consumers, including those in rural areas, have a fair and reasonable opportunity to purchase its programming.[12] That is why it

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[11] Singer, supra at § 48.15

[12] In fact, HBO has a long history of using multiple technologies to distribute its services, including cable (continued...)

entered into the USSB agreement which provides for multiple distributors of the HBO services in rural areas and in all areas.

The Justice Department has considered the breadth of Section 628(c)(2)(C) and concluded that the provision:

> prohibits exclusive arrangements between program vendors and cable operators, but does not expressly prohibit such arrangements between programming vendors and a non-cable firm such as USSB.[13]

This conclusion is logical. The Act and the legislative history give no indication that Congress believed there was a problem with exclusive contracts between programmers and DBS operators or that Section 628 should encompass such contracts.[14] To the contrary, Congress recognized (as the Commission has recognized) the general principle that exclusivity is pro-competitive.[15] Congress enacted the program access provision

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[12](...continued) television, MDS, MMDS, C-band satellite dishes, video cassettes, and SMATVs.

[13] 58 Fed. Reg. 60,675 (1993) (emphasis added).

[14] Prohibiting exclusivity between programmers and DBS operators would be contrary to the Commission's own finding that Section 628 applies to exclusivity between vertically integrated programmers and cable operators. In the First Report and Order in this proceeding, the Commission found programmer-cable operator exclusive arrangements to be a "key area of concern." 8 FCC Rcd 3359, 3378 (1993) ("Order"). The Commission noted that competitors to cable had "been unable to secure certain programming at all because programming vendors have exclusive contracts with cable operators, even in areas not currently served by cable." Id. (emphasis added).

[15] See S. Rep. No. 92, 102d Cong., 1st Sess. 28 (1991); 138 Cong. Rec. H6537 (daily ed. July 23, 1992) (statement of Cong. Schaeffer); 138 Cong. Rec. H6536-37 (daily ed. July 23, 1992) (statement of Cong. Fields); see also Syndicated Programming Exclusivity, 3 FCC Rcd 5299, 5309 (1988) ("Syndex").

only because it believed there was an extraordinary circumstance that justified an exception to the general rule, i.e., Congress' view that cable operators had exercised market power to extract from programmers terms and conditions that harmed cable's competitors.

In its consideration of the 1992 Cable Act, Congress found no record of abuse in the relationship between programmers and DBS operators. Nor could it have done so, since the DBS business had not yet begun. Moreover, it is not plausible that NRTC, through its relationship with DirecTv and General Motors, needs the government to protect it against competition from USSB. In the absence of a record of abuse, the FCC should not take the extraordinary step of limiting private contractual rights between DBS operators and programmers.

II. The HBO/USSB Contract Promotes The Public Interest

A. The HBO/USSB Agreement Promotes Consumer Access to Programming

The HBO/USSB contract will expand consumer access to HBO's services. The USSB programming and the programming that will be distributed by NRTC (pursuant to its agreement with DirecTv) are delivered via the same satellite and can be obtained with the same receive equipment. Any DBS dish that is pointed at that satellite can receive both sets of program offerings. Dish owners who subscribe to the NRTC package simply have to call USSB to subscribe to any or all of USSB's program services. It is the common practice among C-band dish owners to subscribe to multiple program services from multiple C-band providers.

Moreover, USSB's "Open Retail Policy" provides that there will be multiple retailers from whom consumers may choose to obtain the HBO services.[16] Thus, NRTC's claim that "USSB is now the 'only deal in town' for DBS distribution of HBO"[17] is simply not true.

In fact, NRTC's interpretation of program access would require the Commission to reduce program diversity. There are a limited number of transponders on the 101° West Longitude satellite. NRTC urges a rule that would result in the same program service being delivered on the same satellite by two different transponders. Such wasteful duplication is not only contrary to the Commission's longstanding goal to promote program diversity, it violates the Commission's spectrum efficiency policies[18] and likely would reduce the competitiveness of DBS vis-a-vis cable and other distribution technologies.

B. The HBO/USSB Agreement Promotes Competition

The HBO/USSB agreement provides very limited exclusivity. It does not give USSB exclusivity against MMDS, SMATV, C-band

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16 See Ex Parte Response to Ex Parte Presentation By the National Rural Telecommunications Cooperative, Appendix 1, filed by USSB on January 21, 1994 ("USSB Ex Parte").

17 NRTC November 19 Ex Parte at 6.

18 See, e.g., In the matter of Spectrum Efficiency in the Private Mobile Radio Bands, 6 FCC Rcd 4126 (1991); In the matter of Parts 2 and 22 of the Commissions Rules (Refarming Initiative), 3 FCC Rcd 7033, 7041 (1988).

satellite distributors, cable operators, DBS distributors at other orbital slots, video dialtone providers, or any other distributors. As noted above, the HBO/USSB agreement provides for multiple distributors in all geographic areas. Thus, NRTC's assertion that "[n]o other DBS distributors can obtain the same programming from Time Warner ... at any price"[19] is plainly incorrect. For the same reason, NRTC's claim that the HBO/USSB agreement results in "[o]ne-distributor-per-technology"[20] is false.

Moreover, exclusivity can enhance competition by allowing a distributor to distinguish its product from its rivals. DirecTv/NRTC will offer approximately 150 channels of programming to consumers.[21] By contrast, USSB will offer up to approximately 30 channels. The Justice Department has recognized that it is necessary for USSB to differentiate its product in order to compete in the DBS business:

> The effects of DirecTv's proposal on competition among DBS providers is not entirely clear. DirecTv will ultimately be in a position to sell approximately 150 channels of programming, as opposed to approximately 30 for USSB. <u>If DirecTv were able to offer all of the attractive programming that was available to USSB, competition between DirecTv and USSB might be impaired</u>.[22]

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[19] NRTC March 4 <u>Ex Parte</u> at 3.

[20] <u>Id</u>. at 22-24.

[21] NRTC November 19 <u>Ex Parte</u> at 2.

[22] 58 Fed. Reg. 60,675, n. 9 (1993) (emphasis added).

Furthermore, program differentiation will in no way harm consumers because DirecTv and USSB co-own the satellite distribution system and will employ the same receive equipment; thus, consumers will be able to obtain programming from either source merely by dialing an 800 telephone number.

III. HBO Has Legitimate, Pro-competitive Business Reasons For Entering Into the Exclusivity Provision in the USSB Contract

NRTC asserts that HBO's actions are motivated by a desire to protect the Time Warner Cable systems from DBS competition. That is pure nonsense. If HBO wanted to protect Time Warner Cable systems from DBS competition, it would not distribute its services via DBS. The very existence of HBO's contract with USSB disproves NRTC's assertion. In effect, USSB is a national overbuilder that will compete head-on with every Time Warner Cable system in the Continental United States. NRTC's theory that HBO is engaged in a conspiracy to kill DBS by providing its services only to USSB, which NRTC perceives to be the weaker of the DBS providers, is similarly ridiculous. HBO's contract with USSB will <u>enhance</u> USSB's ability to compete and thereby <u>strengthen</u> the overall competitiveness of DBS. By seeking to deny USSB the ability to differentiate its product, NRTC would <u>weaken</u> USSB as a competitor and ultimately would establish itself as the sole DBS distributor in its service areas.

NRTC also incorrectly asserts that HBO entered into the exclusive arrangement with USSB "specifically for the purpose of blocking competition by NRTC" and other DBS distributors.[23] To the contrary, HBO had a number of legitimate, pro-competitive business reasons for entering into the limited exclusive distribution arrangement with USSB, including the following:

- USSB, in exchange for limited exclusivity, expressed a strong desire to aggressively market and promote all HBO's services.[24] USSB's enthusiasm was significant because subscription services are to a large extent driven by marketing. Moreover, USSB and its parent company, Hubbard Broadcasting Inc., have a distinguished record as distributors of programming. By contrast, NRTC has a very poor record of distributing HBO's services. HBO has authorized 21 national distributors of its services to C-band dish owners, including NRTC. Although the C-band business has grown rapidly in the previous two years and the majority of HBO's distributors have shown impressive growth in HBO and Cinemax subscriptions, NRTC has had extremely minimal growth. For example, in 1992 NRTC accounted for only 1.4% of HBO's new C-band subscriptions. By comparison, HBO's top three C-band distributors in 1992 accounted for 54% of its new C-band subscriptions. Similarly in 1993, NRTC accounted for only slightly over 1% of HBO's C-band subscriptions, while HBO's top three C-band distributors generated over 56% of the new C-band

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[23] NRTC March 4 Ex Parte at 2.

[24] The Supreme Court recognized the legitimacy of such a reason for exclusive arrangements in Continental TV. v. GTE Sylvania, 433 U.S. 36 (1977) when it said that suppliers can use exclusive arrangements to induce distributors "to engage in promotional activities." Id. at 55.

subscriptions.[25] Furthermore, the ratio of HBO and Cinemax sales among NRTC customers is extremely low. Among all C-band dish owners that purchase programming, approximately 65% purchase HBO and approximately 54% purchase Cinemax. However, among NRTC customers, less than 35% purchase HBO and less than 25% purchase Cinemax. Given this record, and the large geographic region covered by NRTC (and the attractiveness of its rural areas for C-band dish sales), it is understandable that HBO would prefer to give limited exclusivity to USSB in order to encourage USSB to market its services in all geographic areas, including the NRTC service areas.

- The HBO/USSB agreement provides for multiple distributors of the HBO services in all geographic areas. Moreover, since all consumers, including those in rural areas, will have access to HBO's services from competitive providers, the HBO/USSB arrangement gives consumers a choice of providers. By contrast, NRTC wanted to be the exclusive DBS distributor of the HBO programming in its service areas.

[25] It is worth noting that, despite NRTC's claims that it is the entity most likely to bring programming to rural America, only 211 of approximately 800 NRTC member co-ops have actually sold any HBO services.

- HBO distributes five feeds of the HBO service[26] and three feeds of Cinemax.[27] These multiple feeds afford time and program diversity and significantly enhance HBO's ability to attract and retain customers. HBO has found that where a distributor offers multiple feeds of its services the rate at which subscribers disconnect the services drops dramatically. Thus, it is a considerable advantage to HBO, as well as its subscribers, when its distributors offer multiple feeds of its services. USSB recognized the benefits of delivering multiple HBO feeds and readily agreed to carry all the feeds of HBO and Cinemax in exchange for limited exclusivity. NRTC's interest was in carrying only one HBO channel, a distinctly inferior outcome for both HBO and future NRTC subscribers. By contrast, the HBO/USSB agreement ensures that all subscribers (including the NRTC subscribers) will have access to the full complement of HBO and Cinemax channels.

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[26] The five feeds include an east coast feed and a west coast feed, which provide consumers with three hour time diversity, and three "multiplex" feeds. A "multiplex" feed contains all the programming that is aired on the primary HBO feed for the month, but counter-programmed to provide consumers with even further time and program diversity.

[27] The three Cinemax feeds include an east coast feed, a west coast feed, and one "multiplex" feed.

IV. Conclusion

The Commission properly concluded that the Act's exclusivity provisions apply only to arrangements between vertically integrated programmers and cable operators.[28] As a legal matter, that conclusion is compelled by the language and legislative history of the Act. As a policy matter, the Commission should adhere to its longstanding view that exclusivity promotes competition and program diversity. It should not limit this normal "competitive tool"[29] in the absence of an extraordinary record, which does not exist here, that exclusivity between vertically integrated programmers and DBS operators would diminish competition and consumer welfare.

Respectfully submitted,

HOME BOX OFFICE, INC.

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Its Attorneys

April 15, 1994

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[28] See Order at 3390. See also, 47 C.F.R. § 76.1002(c)(1)-(2).

[29] Syndex at 5309.